Mr. R. V. LeSueur.

CA2ALQG
1945T78
V.33

The Province of Alberta

IN THE MATTER OF "THE NATURAL GAS UTILITIES ACT"

—and—

IN THE MATTER OF an Enquiry into Scheme to be adopted for Gathering, Processing and Transmission of Natural Gas in Turner Valley

G. M. BLACKSTOCK, Esq., K.C., *Chairman*

Dr. E. H. BOOMER, F.C.I.C., *Commissioner*

Session:

CALGARY, Alberta September 4th, 1945

VOLUME 33

Digitized by the Internet Archive
in 2019 with funding from
Legislative Assembly of Alberta - Alberta Legislature Library

I N D E X

Volume 33

Sept. 4th, 1945.

WITNESSES	Page
Discussion	2541
R. D. MERCER (Continued)	
Direct Examination.....	2546
Cross-Exam. by Mr. Fenerty.....	2572
Cross-Exam. by Mr. Steer.....	2591
Cross-Exam. by Mr. McDonald.....	2615

E X H I B I T S

No.		
98	Submission by Royalite Oil Company Limited in respect of Cost of Delivering Wet Gas to the Natural Gasoline Plant (R-2).....	2546
99	Submission by Royalite Oil Company Limited in respect of Price to be paid for Gas to be re-pressured or conserved in Turner Valley or Bow Island fields by Royalite Oil Company Limited..	2553
100	Agreement between Royalite Oil Company Limited and Canadian Western Company, 1921.....	2594
101	Agreement between Royalite Oil Company Limited and Canadian Western Company, 1925.....	2594

: : : : :

THE CHAIRMAN: I understand, Mr. Steer, that your witness will not be called this morning.

MR. STEER: Yes sir. Mr. Martin was being called for the purpose of establishing what might be done in the way of an extension to the Girbitol system as a substitute for the present Seaboard system. During the summer the Canadian Western engineers and the Madison engineers got together and discussed that question and I am instructed that there is probably no substantial difference between them on the question of costs, capital costs, if that Girbitol unit was established. So far as operating costs are concerned there is perhaps some slight difference between the two but just what the extent of that difference is, either from the point of view of capital costs or operating costs, will probably be developed when Mr. Stevens-Guille is in the box. Consequently it looks to us that it may not be necessary to call Martin, depending upon what the Madison and Royalite people have to say.

THE CHAIRMAN: Perhaps, Mr. Blanchard, we should discuss your position for a moment.

MR. BLANCHARD: Well, Mr. Chairman, the Criminal Sittings start: on the 24th of September, and I think that the Chief Justice, who is most obliging, will endeavour to have judges available to take criminal cases on the last two days of the week, that is Thursday and Friday of each week, for the weeks of the 24th of September, the 1st of October and the 8th of October. Commencing the 15th of October, I shall not be able to attend these Hearings. I am in the Appellate Division and in the Supreme Court, I expect, for the whole of that week and then the Barr's case comes on on the 22nd of October and will take, I am quite sure, over a week to try. That brings us to

the week of the 29th, part of which I am afraid will be taken up with the Barr's case and I will ask the Board to adjourn the Hearings during those three weeks. I do not like to put my learned friends out or cause them any inconvenience but that is my position.

THE CHAIRMAN: That being so, and if you can make that arrangement, then we will be able to have five straight weeks of Hearings.

MR. BLANCHARD: Yes.

THE CHAIRMAN: That ought to bring us fairly close to the end, I think; I hope.

MR. HARVIE: I pray.

MR. FENERTY: It is going to put me in a most difficult position. As you know, I wrote various counsel that whatever way they arranged matters was all right with me but I did have what I thought was definite advice that Mr. Blanchard would find himself under the necessity of asking for an adjournment, originally from the 17th of September to the 19th of October. Those were the dates that were given me.

MR. BLANCHARD: Yes, that was my impression. At that time we expected the Barr's case to go on, Sir.

MR. FENERTY: On the stregnth of that - I quite appreciate the situation - but on the strength of that Coal Inquiry adjustments have been made and Mr. Morrison, who is my staff and guide as far as accountancy matters are concerned, has now gone to Ottawa on the Coal Inquiry and will not be able to get back here until the 24th of September. I do not know what accountancy matters are going to come up between now and then. We figured we were quite safe until the 17th and I do not know where I fit in now. I only heard this this morning.

MR. BLANCHARD: Yes, I did tell Mr. Fenerty that and I am

very sorry if he may have started in making arrangements accordingly. I did it in good faith at the time.

THE CHAIRMAN: What is disturbing us is that the Hearing is now dragging out so long and that after all there are interests that are very vitally concerned with the determination of the issues. I mean the producer in the field and even the public who may be called upon to pay certain prices for gas. While we want to accommodate counsel as much as we can, we feel we should try to make more progress from now on than perhaps we have been able to make in the last three months. What is there to go on with this morning?

MR. CHAMBERS: The thought occurred to me, Mr. Fenerty says Mr. Morrison will be available as I understand it on the 24th and we can still deal with a lot of accountancy matters from the 24th of September to the 15th of October.

MR. FENERTY: I would like the Board and counsel to accommodate me to the extent of dealing with matters of a non-accounting nature as far as possible in the meantime.

MR. HARVIE: Our submissions will all largely deal with accounting matters but every person has had ample notice for months that we proposed to go ahead on the 10th and carry on right until the finish. It will be most inconvenient to have to change that.

THE CHAIRMAN: You have the right of way on the 10th Mr. Harvie.

MR. HARVIE: It is not only the start but it is the finish.

THE CHAIRMAN: One thing more, from now on we would like if it is possible to stay with the agenda. That is to say when we start an item, finish it. It is going to be most difficult to jump all over the transcript now to find where

a witness began and where he finished. I have tried a little of it and it is not as simple as it should be.

MR. CHAMBERS: I have had the same trouble.

THE CHAIRMAN: If we can keep to the agenda from now on I think it will be a great help, not only for the Board but for counsel also.

MR. CHAMBERS: Just while we are talking about witnesses I would like to confirm a discussion I had with the Chairman of the Board and other counsel engaged. You remember there was some discussion this summer as to a witness I was to call about rate of return and that he would be available this week. We had all those arrangements made and we were advised by him that he would not be available until next week. I have discussed the matter with other counsel and Mr. Harvie was kind enough to suggest I think as well as agree that my witness from out of town might follow his Mr. Teis next week.

MR. HARVIE: Yes.

MR. CHAMBERS: You recall that when we adjourned on the 28th of June I think it was Mr. Mercer was in the box and had been examined in chief in part. He had filed as Exhibit 97 and just completed the reading of a document or report which was entitled "Submission by Royalite Oil Company Limited in Respect of Sharing of Market for Natural Gas and Repressuring of and Conservation of Natural Gas." Now Mr. Mercer had not completed his examination-in-chief and I would suggest that he be returned to the box at this time.

THE CHAIRMAN: That was Exhibit 97?

MR. CHAMBERS: That is right.

MR. HARVIE: Just before we proceed I would like to get as much information in advance of any adjournments or

any weeks we are not going to sit as possible. As I understand it now the thought it that Mr. Blanchard wishes a two weeks' adjournment and as to any other adjournments they will be dealt with later.

THE CHAIRMAN: As I understand it, Mr. Harvie, Mr. Blanchard hopes to be here the weeks of the 17th and the 24th of September and the 1st and 8th of October but does not expect to be here on the 15th, 22nd or 29th of October, is that right Mr. Blanchard?

MR. BLANCHARD: That is right.

DR. BOOMER: That is a three weeks' adjournment.

THE CHAIRMAN: Yes.

MR. HARVIE: So we will adjourn those three weeks.

THE CHAIRMAN: If it can be made two weeks, we will make it two weeks but that will depend on what happens to the Barr's case which is to start on the 22nd.

MR. BLANCHARD: Yes, and I will not know until towards the end of the week whether we are going to finish up or whether we are not.

THE CHAIRMAN: As to the Appellate Court which is on the 15th of October, how long do you expect to be engaged on that?

MR. BLANCHARD: I have some Criminal Appeals, I do not know just how long they will take, Mr. Chairman, and then I have a Civil Appeal and on the 18th a lengthy civil trial which I have arranged for the end of that particular week.

THE CHAIRMAN: Mr. Chambers.

MR. CHAMBERS: Mr. Mercer.

R. D. MERCER, Recalled.

Q BY MR. CHAMBERS: Mr. Mercer, you are still under oath?

A Yes sir.

Q You had, in the previous part of your evidence, put in evidence Exhibit 97, the report to which I have alluded. As I understand it you have prepared another report on behalf of the Royalite Oil Company Limited entitled "Submission by Royalite Oil Company, Limited in Respect of the Cost of Delivering Wet Gas to the Natural Gasoline Plant".

A Yes sir.

Q That is the report known as R-2. Would you read that report, Mr. Mercer, and make any comment as you go along. I will tender that as Exhibit 98.

"SUBMISSION BY ROYALITE OIL COMPANY LIMITED IN RESPECT OF THE COST OF DELIVERING WET GAS TO THE NATURAL GASOLINE PLANT (R-2)"IS NOW MARKED EXHIBIT 98.

THE CHAIRMAN: Had we finished with Exhibit 97?

MR. CHAMBERS: Yes.

THE CHAIRMAN: There was no cross-examination?

MR. CHAMBERS: No.

THE CHAIRMAN: While we are at that, Mr. Chambers, Mr. Stevens-Guille has not been cross-examined on the evidence that he gave when we adjourned in April and has not been cross-examined as to some of his evidence respecting capital expenditures, rate base. That is Mr. Steer, I think, deferred cross-examination on some of those items.

MR. STEER: Yes sir.

MR. CHAMBERS: Just in connection with that point, Sir, it is my intention, subject to the Board's direction, that when the evidence of Mr. Mercer is completed, that Mr. Stevens-Guille will be available and I intend to put him in the box.

R. D. Mercer,
Dir. Ex. by Mr. Chambers.

I have some questions I want to ask him and the thought I had in mind was we might make a general clean-up of Mr. Stevens-Guille.

(Go to page 2548)

THE CHAIRMAN: Then if we finish with Mr. Stevens-Guille perhaps tomorrow morning, what about Thursday?

MR. CHAMBERS: Well I anticipate Mr. Stevens-Guille may take, - well I think in fact he will take all of one day, but if we finish before Thursday I understood from Mr. McDonald that he had a witness or two in connection with the sharing position.

MR. McDONALD: There are one or two items I may want to call witnesses on, and I have made arrangements to follow Mr. Stevens-Guille, or it may be he may take care of some of the evidence that I want to bring out.

MR. CHAMBERS: As I understand it, Mr. McDonald put in Exhibit 89 shortly before the adjournment and I do not think there has been any cross-examination in connection with that by anybody.

MR. McDONALD: No, that is one of the things I have in mind.

Q MR. CHAMBERS: Now, Mr. Mercer, will you read Exhibit 98, and make such comments on it as you wish to make.

SUBMISSION BY ROYALITE COMPANY, LIMITED
IN RESPECT OF THE COST OF DELIVERING WET GAS
TO THE NATURAL GASOLINE PLANT

(a) Charges outlined by Madison Natural Gas Company Limited (Report M-12) for service charges on gathering, compressing and delivering wet gas to Royalite's Absorption Plant.

The various schedules as contained in Madison's Report M-12 have been examined by Royalite with particular reference to Schedule M-12-D which covers the method of computing the charge to Royalite for gathering and compression costs in respect of transportation services relating to wet gas content delivered to Royalite's Natural Gasoline Plant.

It is submitted that Royalite's Natural Gasoline Plant is one of the customers and a member of the public deriving a service from Madison's gathering, compressing and transmission system for whom Madison supplies a service in the delivery of that volume of natural gas represented by:

(i) Plant vapours.

(ii) Natural Gasoline extraction.

(iii) The proportion of boiler and electric plant fuel.

The aggregate of which is converted or metered to obtain the total volume of gas retained and used by Royalite's Natural Gasoline Plant.

Under Madison's Report M-12.....

Q MR. CHAMBERS: Pardon me, Mr. Mercer, if I may interrupt there for the purposes of the record, "M-12" as I understand it is.....

THE CHAIRMAN: Exhibit 81.

Q MR. CHAMBERS: Yes, Exhibit 81?

A Yes.

Q All right, Mr. Mercer.

A Under Madison's Report M-12, shall I refer to that as Exhibit 81?

Q No, that is all right so long as it is on the record.

A Under Madison's Report M-12, costs of the gathering, compressing and transmission of natural gas have been brought down to a cost per thousand cubic feet of gas handled through their system.

It is submitted that the charge to Royalite for services performed by Madison in the gathering, compressing and transmission of natural gas for the Royalite Natural Gasoline Plant be made on the volumes of gas arrived at under the above submitted formula at a rate per thousand cubic feet as proposed

by Madison (and to be set by the Natural Gas Utilities Board).

As the present gathering and transmission system of the Madison Company supplies adequate service to Royalite's Natural Gasoline Plant it is submitted that the charge set for this service should remain constant for a period of five years or until the next hearing of the Natural Gas Utilities Board.

Under (b) of this submission Royalité has shown the anticipated gross revenues from its Gasoline Plant operations for the years 1944 to 1948 inclusive, and has applied thereto the suggested charge for gathering, compressing and transporting wet gas as per Madison's Report M-12, Schedule D. The Madison charge when applied to Royalite's anticipated gross revenues reflects a percentage of 9.44% to 13.7% of such gross revenue for gathering, compressing and transportation costs, which will be in addition to the amount returned to the producer as the producer's share of the natural gasoline content of the gas.

(b) Statement showing Royalite Oil Company Limited Gasoline Plant Revenues, Charges for Gathering, Compression and Transportation and the Percentages of Gathering, Compression and Transportation Charges to Gasoline Plant Revenue.

Estimated Gasoline Plant Revenues.

This is in statement form covering the years 1944, 1945, 1946, 1947 and 1948.

Estimated Gasoline Plant Revenues.

1944	-	$593,905.00
1945	-	$479,447.00
1946	-	$401,291.00
1947	-	$286,787.00
1948	-	$258,414.00

Gathering, Compression and Transportation Charges as per Madison Report M-12 (Schedule M-12-D).

1944	-	$56.084.08
1945	-	$52,438.40
1946	-	$44,770.56
1947	-	$39,364.26
1948	-	$35,412.48

which showed

Percentages of Gathering, Compression and Transportation Charges to Revenues

1944	-	9.44%
1945	-	10.94%
1946	-	11.16%
1947	-	13.73%
1948	-	13.70%

MR. CHAMBERS: Before we leave this Exhibit, the Board will recall that during the sittings in June, I, on behalf of Royalite, made a statement and an admission that Royalite agreed or felt that it should be charged with the transportation costs of that volume of gas which was returned to the North end for drilling purposes, and which had not been charged in the Madison statement. Now in this Exhibit 98, on page 1, where the three things are listed, that is what Royalite says it should be charged with:

(i) Plant vapours.

(ii) Natural Gasoline extraction, and

(iii) The proportion of boiler and electric plant fuel,

we, on behalf of Royalite, say that there should be another

item, Number 4, showing the volume of the drilling gas that is returned to the North end, and likewise that the statement at the end, on page 3, does not take that into consideration, and I would like to have prepared and filed, probably tomorrow if possible, a revised statement, taking that factor into consideration.

MR. BLANCHARD: Mr. Chambers, so that I may understand, that is the cost of gathering that volume of gas which goes back and the cost of sending it back, compressing it, if necessary.

MR. CHAMBERS: Yes, the cost of sending it back has not been included anywhere, I mean, the North fuel line is not in that.

MR. BLANCHARD: No, but compressing to send it back.

MR. CHAMBERS: That is right.

THE CHAIRMAN: What is included under the term "Plant Vapour", is that more than natural gasoline?

MR. CHAMBERS: I wonder if you would mind if Mr. Stevens-Guille answers that?

THE CHAIRMAN: Perhaps we should leave it until he is in the box.

MR. STEVENS-GUILLE: The same definition which we gave the last time that would include the loss through the liquid extraction, and also the vapours which are taken out at the same time from the liquid and burned in the flares.

THE CHAIRMAN: Who would be the owner of those vapours which are burned, flared, who owns that?

MR. STEER: I think it is important that we should understand it and I do not understand what they are.

THE CHAIRMAN: Well we will make a note to get that

from Mr.Stevens-Guille when he is giving his evidence. Mr. Mercer cannot do it, I suppose.

WITNESS: No.

Q M . CHAMBERS: Now, Mr. Mercer, you have prepared, on behalf of Royalite, a further report which is known as "R-3", and it is entitled:

SUBMISSION BY ROYALITE OIL COMPANY, LIMITED IN RESPECT OF THE PRICE TO BE PAID FOR GAS TO BE REPRESSURED OR CONSERVED IN TURNER VALLEY OR BOW ISLAND FIELDS BY ROYALITE OIL COMPANY, LIMITED

A Yes.

MR. CHAMBERS: I would like to tender that as Exhibit 99.

REPORT "R-3" HERE MARKED AS EXHIBIT 99.

Q MR. CHAMBERS: Would you read this report, Mr. Mercer, and make any comments or explanations which you see fit as you go along.

SUBMISSION BY ROYALITE OIL COMPANY, LIMITED IN RESPECT OF THE PRICE TO BE PAID FOR GAS TO BE REPRESSURED OR CONSERVED IN TURNER VALLEY OR BOW ISLAND FIELDS BY ROYALITE OIL COMPANY, LIMITED

(a) Method for use in arriving at the price to be paid to Producers for residue gas to be repressured in the Turner Valley.

As submitted in (b) of Report R-1.....

Q And that is Exhibit 97?

A Exhibit 97.

As submitted in (b) of Report R-1 Royalite Oil Company, Limited is prepared to purchase gas returned to the formation through certain of its wells. In order to ascertain the fair price of repressured gas at the time of repressuring in comparison to the price of gas at the well head it is submitted

that the following factors should be taken into account:

(1) Price of gas at the well head. As the well head price is at present unknown it should for the present time be designated by symbol "P".

(2) Period of discount As supported by evidence submitted, or to be submitted, gas will be conserved and repressured for a period of thirteen years and it will be a further two years before the present gas allowables will not be sufficient to meet the then market demand. It is therefore submitted that the period that will elapse before repressured gas will be marketed is fifteen years.

(Go to Page 2555).

(3) Rate of discount. Taking into consideration the hazards involved such as incomplete recovery at some future date, errors in estimating the date of production and the future value of gas at the time it is again produced, it is submitted that the rate of discount should be commensurate with the elements of risk involved and that a discount rate of 8% would be fair and reasonable in all respects.

(4) Formula. From the three factors enumerated above a stated formula would therefore be:

Present worth of $1.00 payable at the end of 15 years discounted at 8% annually .31524

Price for repressured gas will therefore be:

P x.31524

Example: Taking the present well head price of 2¢ per thousand cubic feet.

Discounted Price 2¢ x .31524 = .0063048

(b) Method for use in arriving at the price to be paid in respect of gas conserved in the Turner Valley (gas purchased to make up the difference between gas produced from gas cap wells and the share of gas cap wells in the market).

As submitted in (c) of Report R-1 (Ex. 97) it is estimated that gas conserved in the gas cap area of the Turner Valley will not be marketed until fifteen years have elapsed after the date of purchase of such conserved gas. Royalite will, therefore, be subject to similar risks as in the case of repressured gas, and in view of this, it is submitted that the purchase price for conserved gas be calculated by the same formula as for repressured gas as follows:

Price for conserved gas P x .31524

MR. STEER: Excuse me, you have two cents multiplied by .31524 equals .0063048. That is really six tenths of a cent is it ?

A Yes.

Q That should be a dollar sign or else your two zeros should come out.

MR. CHAMBERS: But the factor, .31524 is really dollars.

MR. STEER: You are multiplying two cents by .31524.

THE CHAIRMAN: You have to put a dollar sign in front of your .0063048 or take away the two zeros.

MR. STEER: Really should take away the two zeros because you are multiplying two cents by that factor.

A It is six tenths of a cent.

It is further submitted that the price set for repressured and conserved gas once set should remain constant in order that Royalite may receive neither more nor less than the moneys invested in such repressured and conserved gas plus interest on the moneys so invested, and in order that the sale price for repressured and conserved gas received by the producer plus interest for fifteen years will be neither more nor less than if the producer produced and marketed such gas fifteen years hence.

(c) <u>Royalties payable in respect of repressured and conserved gas.</u>

In Report R-1 (Ex. 97) it was brought out that the plan for repressuring and conserving gas involves the physical transfer of residue gas from crude oil wells to certain Royalite wells in the gas cap area and the non-production of gas allowables from wells in the gas cap area. The actual effect is that all residue gas produced from crude oil wells in

excess of these wells' share of market and available for repressuring will be represented by increased gas reserves in the gas cap area. The economic feasibility of the place of repressuring and conservation, so far as Royalite is concerned, rests upon the opinions of the engineers of Royalite that repressured and conserved gas will not migrate from the gas cap to any great extent.

It is therefore not anticipated that gas produced from crude oil wells will again at a later date be produced from crude oil wells by reason of migration from the gas cap area. On this assumption it is apparent that the owners of royalty interests in crude oil wells must accept their royalties at the time of production. This fact is important and appears to influence to a great extent the entire question of royalties. The following suggestions for the payment of royalties are submitted for consideration:

Crude Oil Wells

In most cases the interest of royalty holders in the proceeds of production is expressed in terms of percentage and such royalty holders would receive their percentages on actual proceeds from sales of gas whether for marketed or for repressured or conserved gas. The exception to the procedure of using percentages is the Government of the Province of Alberta which collects a royalty of fifteen per cent or one-quarter cent per thousand cubic feet, whichever is the higher. At present the fifteen per cent rate is in effect but with the institution of repressuring and conserving gas the fifteen per cent rate on such repressured and conserved gas may be less than the minimum one-quarter cent. The use of the minimum one-quarter cent per thousand cubic feet rate would appear to be excessive if the price for repressured or conserved gas

should be less than one and two-thirds cents.

It is suggested that the Province of Alberta be asked to apply the fifteen per cent rate of royalty in respect of all gas produced from crude oil wells and sold as repressured or conserved gas. The result would be that royalty holders (including the Province of Alberta) share with the producers in the discount arising from the sale of repressured or conserved gas fifteen years before it would normally be marketed.

Repressured Gas

Royalite wells selected as input wells for repressured gas are located on what is known as Crown acreage in the vicinity of its natural gasoline plant. Part of the gas produced from Crown and other acreage in the crude oil area on which royalty has been paid is (by repressuring) transferred to Crown acreage in the gas cap area. Seeing that royalty has already been paid, the formula for calculating the purchase price of repressured gas does not contemplate any royalty being paid by Royalite when such repressured gas is again produced for the market, nor does it contemplate the payment of any tax such as that provided for by Sub-section 2 of Section 8 of the Corporation Taxation Act as under Sub-section 3 of Section 8 of this Act "where a well is worked mainly for the production of oil, the natural gas from such well shall not be subject to such tax".

It is accordingly submitted that:

(i) the reserves of such input wells should be now calculated and established;

(ii) proper records be kept of all gas returned to the formation through the input wells, in order to establish the relationship of the repressured gas

to the formation gas;

(iii) when the input wells are produced for market purposes, the gas so produced shall be deemed to be proportionately repressured gas and formation gas and settlement of the royalty, etc. made accordingly, i.e. paid on the formation gas only.

Conserved Gas

In general royalty is payable only on production and at the market value of such production. Technically royalty payable in respect of gas from gas cap wells would cover only gas actually marketed and royalty on conserved gas would be payable only when actually produced and marketed. As has been previously mentioned the result of conserving gas in gas cap wells is the same as if gas was produced up to the share of the market and an amount of dry gas equal to the dry gas equivalent of gas conserved was purchased and physically returned to the same wells by repressuring. Under such circumstances, royalty holders would be entitled to royalty on gas marketed (equal to share of market) but would not be entitled to repressured gas when the same is in turn produced and marketed. It is therefore suggested that each royalty holder be given the privilege, by agreement, of receiving royalty in accordance with the share of the well in the market.

It is accordingly submitted that:

(1) the reserves of Royalite's own gas cap wells should now be calculated and established;

(ii) proper records to be kept of all gas purchased (to meet Royalite's share of the market to cover conserved gas) in order to establish the relationship of the conserved gas to the formation gas;

(iii) when Royalite's gas cap wells are produced for

market purposes the gas so produced shall be deemed to be proportionately conserved gas and formation gas and the settlement of the royalty made accordingly, i.e. paid on the formation gas only.

(d) Bow Island Re-pressuring Agreement

MR. CHAMBERS: Does the Board wish the Agreement to be read ?

THE CHAIRMAN: Unless some wishes it to be read. I do not know why it should be read.

MR. CHAMBERS: The whole Bow Island situation stems from this Agreement and my idea would be to skip some of the recitals and less important paragraphs, but read sufficient to give us the understanding.

(Go to Page 2561)

MR. HARVIE: I do not care whether it is read or not.

THE CHAIRMAN: Do you think it should be read, Mr. McDonald, the whole agreement or part of it?

MR. McDONALD: Yes, I think it should be read. There are some points in connection with it that should be brought out.

THE CHAIRMAN: All right, Mr. Mercer, read the whole agreement.

MR. BLANCHARD: Cannot it be covered, Sir, by cross-examination, or at least those portions?

THE CHAIRMAN: Well, Mr. McDonald has asked that it should be read, Mr. Blanchard, and I think I should agree.

MR. BLANCHARD: Very well.

Q THE CHAIRMAN: Omit the title, Mr. Mercer.

WITNESS:

WHEREAS under contracts heretofore made the Canadian Western Company purchas s from the Royalite Company natural gas produced by the latter Company in the Turner Valley field and distributes same in the City of Calgary and other adjacent municipalities,

AND WHEREAS, owing to seasonal conditions affecting consumption, the natural gas available for distribution in summer exceed and in winter may fall below the demand, and the parties consider it advantageous to arrange for the storage for later use of such excess natural gas by re-charging with said gas the Bow Island natural gas field, which field the Canadian Western Company has the right to use in the manner hereinafter mentioned but upon terms and subject to conditions disclosed to and known by the Royalite Company;

AND WHEREAS it is desirable that the necessary experiments to ascertain the feasibility of so re-charging the Bow Island field be proceeded with at once and that, if said experiments prove successful, the above mentioned project be put into execution,

NOW THEREFORE the parties hereto in consideration of the covenants and agreements herein contained hereby covenant and agree each with the other as follows:-

1. The Canadian Western Company will forthwith after the signing of this agreement and at its own expense erect and complete at Bow Island a pumping station and plant equipped with pumps of two-stage compression and of a capacity to compress a maximum of three million (3,000,000) cubic feet daily and will therewith, and at its own expense, make such experiments and tests as may be necessary to ascertain whether the re-charging of the Bow Island natural gas field with natural gas as aforesaid is feasible; if such re-charging is found to be feasible, the Canadian Western Company will proceed to re-charge the said Bow Island field with and to store therein such amount of said waste or excess natural gas as is delivered to it pursuant to Article 2 hereof and as can economically and practically be transmitted through its mains from Turner Valley to Bow Island, it being understood that in so doing the Canadian Western Company will, at its own expense, enlarge said pumping station and plant at Bow Island, equipping the same with such further two-stage compression pumps and furnishing such plant, machinery and equipment as may be necessary for the said operation of re-charging the Bow Island field and will take all reasonable steps to preserve the natural gas so stored.

2. The Royalite Company will deliver to the Canadian Western Company at the latter's present measuring station or stations in the Turner Valley field such amount of its natural gas as is not required by the said Royalite Company in its ordinary course of business and as will reasonably enable the Canadian Western Company to determine the feasibility of re-charging the said Bow Island field with natural gas for the purposesherein contemplated, and if such re-charging is found to be feasible, the Royalite Company will deliver to the Canadian Western Company at the latter's present measuring station or stations in the Turner Valley field the excess of natural gas which from time to time is not required by the said Royalite Company in its ordinary course of business; it is understood that the Canadian Western Company shall be entitled to use such portion of said natural gas as may be required as fuel in the efficient operation of the compressor plant and equipment. The expression "ordinary course of business" shall include both present and future business and nothing herein contained shall prevent the Royalite Company from increasing or decreasing the amount of natural gas sold by it in the ordinary course of business and whether to present or future customers or from increasing or decreasing its scrubbing capacity or temporarily closing its plant for repairs or otherwise, the intent hereof being that the only obligation of the Royalite Company hereunder shall be to deliver the natural gas which it may from time to time have available over and above its sales, field or other requirements, and which natural gas would otherwise be wasted. The said natural gas shall, if necessary, be scrubbed or purified so that when delivered to the Canadian Western Company it will be of merchantable quality and fit for consumption for domestic

purposes and, in such case, the amount of natural gas deliverable hereunder shall also be limited by the scrubbing capacity of the plant of the Royalite Company which it shall be under no obligation to increase by reason of this agreement.

3. Nothing in the next two preceding paragraphs contained shall be deemed or interpreted to impose upon the Canadian Western Company any duty or obligation to take delivery of natural gas pursuant to this agreement except at such times and in such quantities as the Canadian Western Company in its absolute discretion may determine.

4. The natural gas now present in and recoverable from the Bow Island field shall for the purposes of this agreement be deemed to be the property of the Canadian Western Company; no charge shall be made by the Royalite Company for the natural gas delivered pursuant to Article 2 hereof and no charge shall be made by the Canadian Western Company for the measuring, transporting, compression, re-charging, storing and preserving of the natural gas so delivered as set forth in Article 1 hereof or for the pumps, pipe, plant, machinery, equipment, materials of labour necessary for such operations, but the natural gas which is compressed and stored in the Bow Island field pursuant to the terms of this agreement and whether during the experimental stage herein mentioned or thereafter shall be deemed the property of the parties hereto share and share alike and subject to the provisions hereof. It is understood that the feasibility of re-charging the said Bow Island field, the receptivity and capacity thereof and all matters relating to the actual work of re-charging said field and withdrawing gas therefrom shall, save as herein otherwise specified be left to the sole and absolute determination and discretion of

the Canadian Western Company, which shall not be liable for the failure to re-charge the said field but shall take all reasonable precautions to prevent the escape of natural gas stored there once the re-charging of the said field has been commenced.

5. The quantity of natural gas stored in the Bow Island field and owned jointly by the parties hereto pursuant to Article 4 hereof shall be deemed to be the amount measured into the field, (that is, the amount delivered at the Bow Island compressor station less the amount of gas used as fuel in the efficient operation of the compressor plant and equipment as evidenced by the meter or meters located on the fuel line leading to such compressor plant and equipment) less a deduction of 10% thereof for storage and other losses. The gas delivered at Bow Island hereunder and the gas withdrawn from the Bow Island field shall be measured by a meter or meters, approved before installation by the Royalite Company, furnished by the Canadian Western Company and placed at locations to be agreed upon by the parties hereto. All measurements of gas under this agreement shall be on the basis of fourteen (14) pounds absolute pressure, a flowing temperature of 40° Fahrenheit, a storage temperature of 50° Fahrenheit and .64 gravity subject to periodical correction. The Royalite Company shall have the right to test all or any meters whenever it so desires and if said meters are found incorrect the Canadian Western Company shall correct the same or install new meters satisfactory to the Royalite Company.

It is understood and agreed that all the natural gas delivered by the Royalite Company to the Canadian Western Company at the latter's measuring station or stations in the

Turner Valley field which is not delivered at the Bow Island compressor station (without deducting the 10% or the amount used for compression purposes above mentioned) shall be deemed to have been delivered pursuant to the terms of the contracts now existing between the parties hereto.

6. The natural gas so compressed and stored shall be treated as a reserve and shall be from time to time drawn upon at the discretion of the Canadian Western Company, provided, however, that in no event shall such withdrawals prejudice, impair or affect the full performance of the contracts now existing between the parties hereto or any extensions or renewals thereof or be made at any time when the then existing demand can be met by the Turner Valley field.

7. All natural gas drawn from the Bow Island field by the Canadian Western Company after the compressor station has been put into operation shall be treated as natural gas stored therein pursuant to the terms hereof until such time as the aggregate of the quantities of gas withdrawn equals the amount of gas compressed and stored in the field computed pursuant to Article 5 hereof and until such time the Canadian Western Company shall on the 15th day of each month pay to the Royalite Company as its share for each thousand cubic feet of such natural gas withdrawn during the preceding calendar month an amount per thousand cubic feet equivalent to one-half of twenty-five per cent (25%) of the average price per thousand cubic feet received by the Canadian Western Company for all gas sold by it during the preceding six months' period, provided, however, that the minimum amount per thousand cubic feet so payable to the Royalite Company shall be four (4) cents.

8. The Canadian Western Company agrees to furnish the Royalite Company with bi-monthly statements showing the amount of natural gas delivered at the Bow Island compressor station, the amount of natural gas consumed by the compressors and the amount of natural gas withdrawn from the Bow Island field, together with the meter charts verifying the above, and the Royalite Company shall at all times during the currency of this agreement have free access during business hours to the records of the said pumping or compressor station at Bow Island and to all other records which in any way relate to the performance of this agreement.

9. In the event of any disputes or differences arising between the parties hereto relating to the performance of the terms of this agreement, such disputes or differences shall be referred to a single arbitrator to be agreed upon between the parties hereto, or, if they are unable to agree upon such arbitrator, then such disputes or differences shall be referred to a Judge of the District Court of the Judicial District of Calgary as sole arbitrator in accordance with the provisions of the Arbitration Act of the Province of Alberta and any amendments thereto and in such event this paragraph shall constitute a submission to arbitration under the provisions of the said Act and amendments thereto.

10. Nothing in this Agreement contained shall be deemed or taken to vary, change, alter or amend the contracts heretofore made in respect to the purchase of natural gas between the Canadian Western Company and the Royalite Company.

This Agreement shall enure to the benefit of and be binding upon the respective successors and assigns of the parties hereto.

IN WITNESS WHEREOF the parties hereto have hereunto

caused their repsective corporate seals to be affixed, attested by the signatures of their proper officers, the day and year first above written.

SIGNED, SEALED and DELIVERED)
in the presence of:)

ROYALITE OIL COMPANY LIMITED

"J. H. McLeod"
President
(SEAL)

"R. E. Walton"
Sec-Treas.

THE CANADIAN WESTERN NATURAL GAS, LIGHT, HEAT & POWER COMPANY, LIMITED.

"C. J. Yorath"
President
(SEAL)

"M. Watts"
Secretary

MR. HARVIE: May I ask one question. In paragraph 6, Mr. Mercer, of that agreement, you refer to the full performance of the contracts now existing between the parties hereto or any extensions or renewals thereof or be made at any time when the then existing demand can be met by the Turner Valley field. Are there any other contracts in existence now that affect this agreement?

MR. STEER: What paragraph is that again?

MR. HARVIE: On page 12.

A There are no further agreements in existence relative to the repressuring of gas in Bow Island, Mr. Harvie.

Q Then what would that clause have reference to?

A Any other existing agreements between the Company and the Gas Company.

MR. STEER: The agreement under which gas is delivered for comsumption by the Royalite Company to the

Canadian Western.

THE CHAIRMAN: Is that all?

MR. HARVIE: That is the only question, yes.

THE CHAIRMAN: All right.

THE WITNESS:

(e) Repressuring of scrubbed gas in Bow Island Field.

Under (d) of this submission is a copy of agreement dated 20th August, 1930, between Royalite Oil Company, Limited and The Canadian Western Natural Gas, Light, Heat and Power Company Limited, the main features of which are:

(1) Division of Costs:

Royalite bears costs of production or acquisition of gas, costs of scrubbing and gathering, transportation and delivering into the inlet of the Gas Company's pipelines at a point on the outlet of the scrubbing plant in Turner Valley.

Gas Company bears costs of transportation through its own pipelines to the Bow Island Field and costs of compressing and returning to the formation in that Field.

(2) Value of gas when marketed to Royalite Oil Company, Limited:

Gas repressured in the Bow Island field is owned jointly by Royalite and the Gas Company and the price to be paid to Royalite at the time repressured gas is marketed is one-half of twenty-five percent of the average price per thousand cubic feet received by the Gas Company or four cents per thousand cubic feet, whichever is the greater.

To date gas repressured in Bow Island has been supplied from Royalite wells and the true cost of the venture has con-

sisted of costs that would not have been incurred if gas scrubbed and delivered for repressuring in Bow Island had instead been flared. Under such circumstances, the venture was economically feasible even if the repressuring experiment later turned out to be a failure.

In view of the risks involved in the repressuring plan in Bow Island, Royalite takes the position that it would not be economically sound to incur greater costs in respect of gas repressured in Bow Island than costs incurred for gas repressured in Turner Valley and that the total cost should be the price payable to Madison for repressured gas in Turner Valley as determined by the same formula, which is:

Price for repressured gas - P x .31524

This means that Madison, and, in turn, the consumers of gas would concurrently absorb any costs of gathering and scrubbing gas to be stored in Bow Island. Gas from Bow Island field does not require scrubbing and it is necessary that gas delivered to Bow Island be previously scrubbed, which means that gas marketed from Turner Valley is scrubbed at the time of marketing and repressured gas marketed from Bow Island is scrubbed prior to repressuring. In each case, gas consumers will only once incur the cost of scrubbing.

It is also submitted that, in respect of gas scrubbed and delivered to Bow Island, the true cost of such scrubbing consists only of costs that would not be incurred if this gas was not scrubbed. On the other hand, if the same gas is repressured in Turner Valley, gas consumers would bear the entire cost of scrubbing operations at the time in the future when this gas is supplied to the market. It appears, therefore, that the absorbing of scrubbing costs at the time of repressuring in Bow Island would result in minimum scrubb-

ing costs to the consumer, and in addition, the consumer would benefit from a reduction of repressure equipment capacity in Turner Valley and corresponding lower operating expenses and carrying charges.

Royalite Oil Company, Limited has instructed me to state that Royalite is prepared to continue to operate under the beforementioned agreement of 20th August, 1930, only if the cost to Royalite is not greater than the cost of purchasing gas at the price set for repressured gas in Turner Valley, such price not to exceed a maximum of 3.6¢ compounded annually at 8%, or a maximum price of 1¢ per thousand cubic feet which Royalite is prepared to pay for the purchase of gas for repressuring in the Bow Island field.

MR. CHAMBERS: I have no questions to ask Mr. Mercer at the moment.

THE CHAIRMAN: Cross-examination?

MR. STEER: My cross-examination of Mr. Mercer, Mr. Chairman, will not be dealing with market sharing. Mr. Mercer is here as an officer of the Royalite Company and there are some questions which some counsel are interested in getting answers to from an official of the Royalite and I take it that this probably would be the proper time at which to put those questions to the Royalite Company. The questions which I propose to ask have to do with the relationship between the Royalite Company and the Madison Company prior to the severance off the properties.

THE CHAIRMAN: Well I do not mind or we do not mind in which order it is done, Mr. Steer. Can you go ahead, Mr. Fenerty?

MR. FENERTY: Yes, I might go on with a few questions that I have in mind now.

CROSS-EXAMINATION OF SAME WITNESS BY MR. FENERTY.

Q Mr. Mercer, turning to Exhibit 97, your report R-1, I note the opening statement that I am interested in at the moment "any proposal in connection with the marketing and conservation of gas should be predicated on the theory that each producer of gas share in the available market for gas in the ratio that the gas allowable from each individual well bears to the total gas available for market, subject however to the adjustments hereinafter mentioned." Now as I understand the situation, there are some oil wells operating which necessarily flare their gas today. They are not on the line in any way, that is so is it not?

A That is so.

Q And that apart from blow-down operations and intermittent operations of that kind they are wells that so far as we know, if they are to continue to operate as oil wells, will operate indefinitely in the future with flares, with waste gas. That is so, is it not, as far as we know today?

A Now in my own right I cannot answer that.

Q Well you do know, do you not, that there is today, I wont say wasted, but a flaring of gas in a good many million cubic feet per day?

A I do know that there are certain wells that do flare their gas, yes.

Q And that situation exists apart from intermittent operations such as blowing down wells. In other words, it exists in wells which have not been coupled to the line. You know that don't you?

A Yes.

Q You know that is either because of their position or their pressure or perhaps both in some cases?

A Well I am made to understand that.

Q And we know, do we not, that there are wells in what I might call an intermediate position that have been coupled up to the lines as a result of extensions which have been made and which previously flared gas, you know that don't you?

A Yes.

Q And there are some of those wells substantially further away from scrubbing plants, we will say, than the wells away out that cannot get on the line at all. Pardon me, substantially further away than the inside wells and substantially nearer than the ones out beyond that cannot get on the line at all, are there not?

A Yes, I think I can say that is true, yes.

(Go to page 2574)

Q And it necessarily follows, does it not, that the cost of taking the gas from these intermediate wells by reason of the greater amount of line that is necessary and so on is greater than the cost of some of the close-in wells, that is necessarily so?

A Yes, it follows.

Q And if your suggestion is correct that any proposal in connection with the marketing and conservation of gas should be predicated on the theory that each producer of gas share in the available market for gas in the ratio that the gas allowable from each individual well bears to the total gas available for market, should not all of the wells in that area be coupled up to the line?

A If they are capable of producing to the necessary requirement.

Q And have you any suggestion as to what consideration dictates coupling up some wells to the line and leaving other wells off the line?

A No sir.

Q Can we assume it is an economic situation?

A Well I cannot answer that question, Mr. Fenerty.

Q You see what I am getting at. We have some wells which do produce, we will say, at one cost, that is gas available for market and we have some wells out beyond, that everybody apparently agrees cannot produce gas for the market at any feasible cost, and we have some in between, that can produce at a greater cost than the closer-in ones, - now that means that the cost of production varies in different wells, does it not, for gas for market?

A Yes, the costs of production do vary.

Q Yes, and have you any suggestion as to who bears that variation in cost?

A No sir.

Q You see we are going to have, as I understand it, we are going to have substantial costs in making a market for certain wells that cannot produce as cheaply as others, that is what it comes to, does it not?

A Will you repeat that again, Mr. Fenerty?

Q Let us take these intermediate wells, we are going to have very substantial costs in getting them on to the line, that is right is it not, in order to get them into the gathering system and sell their gas, are we not, that is just elementary.

A Yes, there may be extra costs, yes.

Q Now have you any suggestion at all as to who should bear the cost of creating the market for those wells?

A No sir.

Q Have you any idea as to who ordinarily bears the cost of creating a market for a product where there is an established price for that product?

A No sir.

Q Never heard of the consumer doing it, did you, just talking as man to man, you have never heard of that?

A No, I have not.

Q Outside of a gas inquiry, you never heard of it, did you; just, I was just wondering if you ever heard of that kind of a situation.

A No, certainly not.

Q All right. Now let us go back to these wells which cannot get on the line for some reason and they are blowing gas into the air, as a result of an oil operation I take it, that is the reason they are flaring gas, on account of the oil operation.

A Yes.

Q That is the only kind of operation they have?

A That is right.

Q And as a result of that use of that gas, - I am not going to call it "waste" because it is being used in producing oil, is it not?

A Yes.

Q As a result of the use of that gas the gas reserves in Turner Valley are being depleted, are they not?

A To some extent.

Q Yes, and treating the operation in Turner Valley as a gas operation, do you think that those wells that are blowing this gas off into the air should be penalized or made to share some of the expenses of handling the gas, do you think that would be fair, do you put those wells into a category of that nature?

A I think that is an engineering problem, Mr. Fenerty.

Q I thought it was an economic problem and I was paying you the compliment of trying to discuss some of these things with you, you would not like to express an opinion about that?

A No, I would not.

Q Take the other end, do you think they should be compensated because they are not able to share the market because of their location, have you any ideas on that set-up?

A No, it would depend on what would be recommended.

Q Would it be fair to say that probably the best way to treat them is that they are just an oil operation first, last and all the time, and let it go at that.

A Following the usual practice that would be so.

Q That would be so, yes, and those wells which are in the intermediate position which are now getting on the line but heretofore have flared their gas, would it be equally fair to

say that they are oil operations primarily just as much as the ones out beyond that cannot get on the line, can you make any distinction between those and the ones which are not 100 yards perhaps beyond them.

A If their gas is being produced in such a manner that it can be accepted into the gathering system there is a distinction.

Q But at some expense beyond the normal expenses which there have been in producing gas they can get on the line; but they are producing anyway if they do not get on the line they will flare; is there any difference between that being an oil operation and the ones out beyond that cannot get on the line.

A I would not know.

Q It would seem absurd, would it not, to say that the test of a well, of a company owning a well producing oil, if it is an oil operation or a gas operation is whether he is going to produce his oil in any event, sell the gas if he can and flare it if he cannot, to say that one is a gas operation and that the other is an oil operation, that would be absurd, would it not?

A Yes, primarily it is an oil operation.

Q Now have you any suggestion as to who should share those increased costs of getting those intermediate wells on the line; I am going to suggest to you it is another element in this great problem, what do you think about that?

A The whole matter is a matter of the conservation of the gas and as such if there are any costs in the gathering or handling of the whole set-up it is a matter of costs to the gas.

Q You mean conserving this gas as produced as a result of the oil operation, do you?

A Yes, in handling, the whole problem under discussion is a matter of conserving and extending the life of the, the useful

life of the natural gas in Turner Valley and the costs in that would be chargeable against the gas.

Q I suggest to you that where you are doing that and you are getting conservation of gas, so that you say each one will share in the market, - each of those producers, - that that is a cost amongst themselves, that this is for the purpose of letting them share the market, is it not, that is what it is now, it is sharing the market?

A Yes.

Q Then is it not necessarily a cost to be apportioned amongst those sharing the market, would you not think, what do you think about that?

A Well offhand I would not want to answer without some consideration.

Q What?

A I would not want to answer without some consideration.

Q I see. Would you go as far as to say it sounds reasonable offhand, just offhand?

A That those costs be borne by the producer, is that your suggestion?

Q Either the producer, who insists on producing, and those who are going to share in selling the gas, somewhere between them, that sounds reasonable, would it not?

A I would not want to say offhand without studying it.

Q I can understand you would not want to say but are you in a position to express any opinion whether it sounds reasonable or not?

A Not a reasonable opinion at the present time.

Q I see. We will leave it at that.

Now again, in that Exhibit 97, at page 3, paragraph "B", where you refer to:

"It is anticipated that gas will be available for repressuring from the Madison system and Royalite is agreeable to undertake the repressuring of this gas in certain of its wells, the same to be marketed by Royalite at some date subsequent to the repressuring. For purposes of this submission it is estimated that this date will be 15 years after the date of repressuring, which is supported by evidence already submitted or to be submitted."

And again in Exhibit 99, pages 2 and 4, you refer again to that situation and you base your calculation of the price to be paid to the producer, you work out a discounted figure because of this fact that this gas will be used in 15 years' time; now it seems to me, Mr. Mercer, and perhaps I am wrong, that in adopting this suggestion that the price to be paid by Royalite to the producer should be discounted because it will not be sold for 15 years, that you are necessarily adopting the position that all of this gas will be taken into consideration and that everything in connection with that will be paid for when the gas is sold 15 years from now, is that your position?

A Yes, if I follow your question, there will be a purchase at the present time at a discounted rate and in 15 years time that gas will be purchased and paid for through the Royalite Company.

Q So I take it by that, that you are of somewhat the same idea as Mr. Davis was, of Buffalo, that the time to pay for these things and the time to find out what you are to pay for them is when they are used and paid for by the people who use them.

A That is so, yes.

Q These figures you have worked out, this discount, is on the basis that this repressured gas and conserved gas will not be required for use for fifteen years ?

A That is so.

Q And have you any suggestions as to who should pay the cost of providing a supply fifteen years from now ?

A I would follow that the consumer would pay for it.

Q The consumer of that gas ?

A Yes.

Q That is used in fifteen years. Is that the one you are talking about. Let us take the case of Mr. John Smith who happens to be a Bank Manager and he comes here today and he is transferred in five years to some other place. You would not suggest he should pay any part of it would you ?

A It is a long time service that is going to be beneficial to the community and as such it would seem all consumers -

Q Beneficial to -

MR. CHAMBERS: Let him explain.

A Should bear the cost of supplying that benefit.

Q MR. FENERTY: The City of Calgary does not pay for any gas except such as is used under some boilers, perhaps down at Victoria Park. You are not going to get it out of the City of Calgary or the City of Lethbridge, a corporate entity ?

A No.

Q You are going to get it from the ultimate consumer. You are going to get it from Thomas Smith or John Brown. Is that right ?

A That is right.

Q And we agree that the man who uses it should pay for it, don't we ?

A Yes.

Q And that is going to be some person, corporation or scientific body in fifteen years from now that is going to use it ?

A That is when the gas will be used.

Q And those are the individuals who should pay for that gas are they not ?

A Quite.

Q Now Mr. Mercer I am a little interested in this Bow Island Agreement and there were apparently some expenses incurred by Royalite Company in connection with those operations under which the repressured gas became the property of the Royalite and the Canadian Western Company in equal shares ?

A That is so.

Q And who absorbed those expenses ?

A The Royalite Company absorbed costs, whatever costs there were, up to the point of -

Q And I take it the reasons for it were, one, that it was an interesting experiment and would determine what could be done in the future and, two, that when that gas was sold and withdrawn they would get paid for their share ?

A That is right.

Q So that up to the present time the Royalite Company has adopted the policy which apparently seemed sound to them, that in the case of repressuring, the compensation for it would come when the gas was used ?

A That is so.

Q And can you see any reason for departing from that principle today, can you, leaving out the fact that this is a utility. Do you see any sound reason for departing from it ?

A Well it would seem to me there is no departure to the extent that Royalite will wait fifteen years until such time as this repressured and conserved gas is sold before they recover any

of their costs.

Q Do you agree with me that there should be no departure from that principle. That is that the cost of it and the payment of those costs and everything should be borne by those who use itatthe time when it is used ?

A Well as I said before, Mr. Fenerty, in so far as the Royalite is concerned I do not think there has been any departure.

Q I do not say there was. You agree with me now that there should be no departure from that principle do you ?

A Following that submission, yes.

Q But you do make the submission that there should be some payment of scrubbing costs now by somebody although the gas is not used, don't you ? I thought I read that in this submission.

A Yes, you did. There has been a change of course since an agreement was entered into between Royalite and the Canadian Western Company to the extent that scrubbing facilities are now a utility. There is a sharing of the market and not only is it Royalite gas going into this repressured gas, but it is other producers. To those extents there are differences Mr. Fenerty.

Q Now then whether that suggestion that there should be some payment by somebody for some scrubbing costs - now in the case of Bow Island where you have to scrub to repressure and you use that, as I understand it, you use that fact that you must scrub the Bow Island gas as a reason why scrubbing costs of the Turner Valley repressured gas should be considered. Now am I right about that now ?

A No as I see it this way in utilizing Bow Island repressuring you will save expenditures relative to repressuring in Turner Valley. You do have to scrub the gas prior to repressuring in Bow Island which is not a fact in repressuring in Turner Valley but you do have to scrub the gas ultimately for

consumption as produced from Turner Valley. There is no duplication of service in a way between the two systems or proposals.

Q I am not sure I understand that, but in any event I will leave it with this - that whether your submission as to some scrubbing costs being paid now for instance in connection with repressured gas in Bow Island, I take it from what we have gone through before that you agree with me that that is not a problem of the man who is burning gas in his furnace today and is gone tomorrow. This John Smith, the banker, I talked about.

A To the extent he will not be here fifteen years from now to consume the gas if I follow your question.

Q Again it is the problem of the man who uses it ?

A Yes.

Q And if that is so does it not follow in your opinion this whole basis of repressuring and conservation is necessarily conservation I mean in order to prevent flaring and so on, necessarily a problem of the industries that created that. That is, of the oil, or the natural gasoline, or both industries. Is that not the logical conclusion of everything we have been talking about ?

A I do not know that I follow you there Mr. Fenerty.

Q You do not know that you follow me that far ?

A No.

Q I see.

THE CHAIRMAN: If it had not been for the production of oil these problems would not be here. Therefore it is an oil producers problem, that is your question.

MR. FENERTY: Yes, as I say the oil industry today in flaring twenty-five million feet or whatever it is, is increasing that problem today and they say because that twenty-five million feet is being flared today you should pay an

increased price for gas today. I will leave that.

THE CHAIRMAN: One observation that Dr. Boomer has made to me and I want to get it on the record. If it had not been for the search for oil there would be no gas in Turner Valley today either.

MR. FENERTY: That is probably quite correct. I do not think there is any question about that.

THE CHAIRMAN: Just where do the two lines cross ?

MR. FENERTY: Let me put it another way. If it had not been for the search for oil, the oil industry would not have a waste product.

THE CHAIRMAN: And Calgary would not have any gas.

MR. HARVIE: And we would have no problem at all.

Q MR. FENERTY: Now Mr. Mercer, in Exhibit 98, at the bottom of Page 1, "It is submitted that the charge to Royalite for services performed by Madison in the gathering, compressing and transmission of natural gas for the Royalite Natural Gasoline plant be made on the volumes of gas arrived at under the above submitted formula at a rate per thousand cubic feet as proposed by Madison (and to be set by the Natural Gas Utilities Board)." Are you intending to suggest that, Mr. Mercer, the costs of transmitting this wet gas from the wells to the absorption plant as ascertained by Madison should be taken into consideration and some charge in addition to that cost made by way of profits to Madison against the Royalite Company?

A The Madison Company as a utility company have performed a service and Royalite submits they should pay for that service.

Q You are not suggesting that the Royalite Company should be charged the entire cost of transporting all of that gas to its plant, plus something for profit, are you ?

A Certainly the Madison Company has performed a service as a

utility company. They have their capital investment and so on. It seems to me as a customer, Royalite should pay whatever rate would be set for the services rendered, taking everything into consideration.

Q You do not get what I am getting at. I am going to suggest to you first of all we have an oil company that has a by product down stream from its separator, some wet gas from which natural gasoline can be extracted and then that wet gas - there is a market for it. That wet gas is taken through gathering lines to its absorption plant and in many cases you had that market apart from any dry gas market. That went on for years. Wet gas going to an absorption plant, the natural gasoline being extracted, a certain proportion of it, and the residue flared. That went on for years didn't it ?

A That is right.

Q And I am suggesting to you that you got another step in the chain. You have got a volume of wet gas that is taken to an absorption plant which would go there anyhow, whether any citizen in Calgary is burning gas, and you have a commercial operation there a revenue, and you have a waste from that which is flared if there is no market and sold if you can get any. Now I am asking you if in view of that when you referred to that cost of gathering and transporting, are you suggesting that the charge for that, bringing that wet gas to the absorption plant where it is treated as a commercial operation, that all of the cost of that should be charged to the gasoline operation or do you propose to divide those costs with the dry gas operation down stream ?

THE CHAIRMAN: We are going to give Mr. Mercer a few minutes to think about that.

(At which time the Commission adjourned for a few minutes)

Q Mr. Mercer, when we adjourned I was following the chain of circumstances of the fact that wet gas coming out from the separator at the well down through the gathering lines to the absorption plant, and having a certain amount of gasoline extracted from it and with, I suggest, so far as the absorption plant at least is concerned, a waste of dry gas, which may or may not become a waste, depending whether there was a market for it. Now I was suggesting to you, I was asking you rather, whether you do say that the cost of getting that wet gas from the well to the absorption plant, whether that should be borne by the absorption gasoline industry?

A Only to the extent that the service has been rendered to the gasoline industry.

Q You would make an apportionment of costs between what, the gasoline industry and the dry gas industry?

A Yes, according to the submission.

Q Now then, I note amongst other things that the well owner participates in the commercial undertaking, that recovery of wet gas, and he gets for his wet gas the value of a fraction of the gasoline recovered, doesn't he?

MR. CHAMBERS: You said wet gas.

Q MR. FENERTY: Recovery of wet gasoline. And he gets for his wet gas the value of a fraction of the gasoline recovered doesn't he?

A According to the contract that he holds with the plant operators.

Q Yes. We will say perhaps 20% of the value?

A Yes. There are contracts of that kind.

Q And do you suggest that the well owner who gets 20% of the value of the wet gas recovered should participate in the cost of conveying that wet gas to the absorption plant?

A Under the contract in effect for the plant operators, they would bear no cost.

Q But as part of the utility operation, do you think that the well owner should participate in that cost, never mind the present contract?

A No.

Q I see. Now you do think that the user of dry gas should participate in it, do you?

A In the gathering of the gas?

Q Yes?

A Yes.

Q Is it fair to say that you think that everybody who gets something out of it should participate except the well owner, is that it? Is that your position?

A Well the well owner has a product which is a useble product and he has made a delivery of his product at a certain point and been paid for it.

Q Where has he made delivery of it?

A He has made delivery of it at his well head.

Q To whom?

A To the gatherer of the gas, which in this case is a utility company, for the ultimate distribution to market.

Q Well, you do not think that the well owner should participate in the cost, although he gets something out of it?

A In this case, no.

Q I see. Now we have got this far, that you think that these costs should be divided between the gasoline industry and the dry gas industry, am I right?

A To the extent that the gasoline industry have received a service.

Q And the reason you refer to the gasoline industry having received services is because that industry has divorced itself from the dry gas operations, isn't it?

A Yes, to the extent of recovery of the petroleum products.

Q And have you any suggestions to make as to why, in setting up the present company's structures, the dry gas industry did not make arrangements to get its production down stream from the absorption plant?

A I do not know anything about that.

Q That is the point where the market originates, down stream from the absorption plant, that is right isn't it? It is a dry gas that they handle, that they sell?

A The gas available for market certainly has gone through a process.

Q Yes. And I think Mr. Kirkpatrick said that the Madison Company was dedicated, I think, is that the right word, to the dry gas industry, that in effect is the wording, that is right isn't it? Perhaps you were not here when that discussion took place?

A I was not here, I do not think.

Q Well, do you know yourself of any reason why the Madison Company did not start its operations down stream from the absorption plant?

A No.

Q You do not know anything about that?

A No.

Q That is a policy dictated, perhaps a head office policy, something like that. You did not participate in that?

A No, I did not.

Q Allright. Now then, when you say that the costs of this

wet gas being conveyed from the well to the absorption plant should be shared by the dry gas industry and the gasoline industry, I understand you to say that it should be apportioned om a volume basis?

A Yes, to the extent of the volume of the service which has been rendered to the Royalite Company.

Q And we have had evidence, Mr. Mercer, from Mr. Kirkpatrick, of the Madison Company, who said he was a former employee of the Royalite Company, my understanding of his evidence was that prior to separation of these functions, that is, the taking over by the Madison Company of the dry gas industry and some other things, that statements were prepared allocating costs of gathering wet gas between the several departments of the Royalite Company, that is, the gasoline and the dry gas industry, on the basis of 60% and 40%, that is right, is it not?

A Well.....

MR. CHAMBERS: Well you might be right but I am not very definite on that.

MR. STEER: That was Mr. Latham's evidence.

Q MR. FENERTY: 60 to the dry gas and 40 to the gasoline operations. Now do you know yourself if that was so?

A Certain statements have been prepared primarily for distribution of incomes of the several units of the Company for computation of income tax.

Q Yes. I see. And do I understand that you are now recommending a computation on the basis of volume?

A After having considered the matter of the, the whole matter having now come up and been gone into, we feel that the submission as made is a more equitable one than what we have used in the

post for inter-departmental use.

Q And did your change of views take place about the same time as Mr. Kirkpatrick's, do you know?

A We studied it pretty well together.

Q And prior to this question of this separation and the subsequent formation of the public utility, your opinion and the opinions of your officials generally was that the 60-40 basis was the correct one, wasn't it?

A For the purposes of the gas operation itself it was felt that it was equitable at the time, having no bearing outside of the Company.

Q Now, you mentioned income tax. You would not, of course, be making a charge against the company for the Royalite Company for income tax purposes which was not equitable, would you?

A The only thing when I say income tax, as you understand, in the computation of income tax on producing gas, certain allowances for depletion and so on are applicable. You must make, with a Company like Royalite, with diversified operations, you must make a distribution of income so as to arrive at that certain reserve or allowance. That was why we made that on that basis, which was agreeable to income tax authorities.

Q So that this change over is in effect a joint idea of yours and Mr. Kirkpatrick's?

A Of the accounting organization, and the organization of Royalite.

Q And would you mind telling me whether or not before deciding on that change you gave any consideration to its effect from a public utility point of view?

A It was considered that it more closely apportioned the cost for the service that would be rendered.

Q Well, just let us discuss that frankly, is it fair to say that had it not been for the situation we have today, with this dry gas operation coming as a public utility, and with this Inquiry, that so far as you know the change would never have been made, is that a fair way to put it?

A That would have been a matter of policy in the operations of the Royalite Company.

Q So far as you know you are the one that got this idea, you say. I say so far as you know the change would not have been made, is that fair, just you yourself?

A I would not want to go that far, Mr. Fenerty, no, that it would not have been made.

Q Had you ever contemplated it prior to this situation arising?

A The matter had not come up.

Q What is that?

A The matter had not come up. It was only in discussing and going over these problems for the formation of the public utility company.

Q Is this fair, the possibility of making this change came up somewhat because of the situation in prospect.

A Quite, yes.

Q Yes. If the Court please, I think I will leave it there. Mr. Steer had mentioned that he proposed to go into the question of those statements, and there is no use of us duplicating it. As long as he is going into it I won't bother.

(Go to page 2592)

CROSS-EXAMINATION OF THE SAME WITNESS BY MR. STEER.

Q Your connection, Mr. Mercer, with the Royalite Company dates from when?

A 1930.

Q Have you made any study of the early history of the company?

A Only insofar as surveying general matters of the Company after I took my present position.

Q My understanding is that the Royalite Company had its inception by taking over the three original Royalite wells that had been drilled by a company controlled by Mr. Dingman, do you know about that?

A Well whether Mr. Dingman controlled the Company I would not know. They took over properties which comprised wells presently known as Royalite 1, 2 and 3.

Q Yes.

MR. HARVIE: Calgary Petroleum Products Limited.

Q MR. STEER: And those wells, 1, 2 and 3 were drilled in a search for oil. Would you know that?

A I think I could say yes to that.

Q And in that search for oil, wet gas was discovered.

A Yes sir.

Q And an absorption plant was built back prior to 1921 for the purpose of obtaining the naphtha products from those wells. Is that right?

A Certainly there was a plant there for the extraction of the naphtha products, yes.

Q Yes. Now then, as I understand it again there was a Gas Inquiry made by the Public Utilities Board and an Order was made in October, 1921, and the effect of that Order was to direct the Gas Company to augment its gas supply, have you any knowledge of that?

A No sir.

Q Have you any knowledge of an agreement following that Order of October 1921 under which this residue gas from the Absorption plant, which was treating the wet gas from 1, 2 and 3 Royalite wells, the residue gas was delivered over to the Gas Company to augment its supply. Do you know about that?

A Is that agreement in writing, 1925?

Q Well there was an agreement of 1921.

A Oh, the original agreement.

Q The original agreement.

A I know generally there was an agreement.

Q These Royalite 1, 2 and 3 wells were in Section 6 were they not?

A Yes sir.

Q And that original 1921 agreement had to do only with gas that resulted from operations in that Section 6.

A I cannot say offhand about that original agreement, sir.

MR. STEER: I do not recall whether that agreement is in, sir.

THE CHAIRMAN: I do not think so.

MR. STEER: I think perhaps we ought to have a look at it and if I may do so, I will hand up some copies. I have not them here but I would like to put in the agreement of 1921 and also the agreement of 1925.

MR. HARVIE: Will those be marked now?

THE CHAIRMAN: Do you want a number for them now, Mr. Steer?

MR. STEER: That will be satisfactory, sir.

THE CHAIRMAN: These are agreements between the Royalite Company and the Gas Company?

MR. STEER: Yes sir.

MR. HARVIE: They will be before the Royalite.

The Calgary Petroleum Products.

MR. STEER: No, the agreement of 1921 was with the Royalite Company. The reason I have not these here, sir, is they are coming down by express and they have not arrived yet.

AGREEMENT BETWEEN THE ROYALITE OIL COMPANY LIMITED AND THE CANADIAN WESTERN NATURAL GAS, LIGHT, HEAT & POWER COMPANY LIMITED, dated October 1921, IS NOW MARKED EXHIBIT 100.

AGREEMENT BETWEEN THE ROYALITE OIL COMPANY LIMITED AND THE CANADIAN WESTERN NATURAL GAS, LIGHT, HEAT & POWER COMPANY LIMITED, of 1925, is NOW MARKED EXHIBIT 101.

Q Then there was a fire shortly prior to the agreement of 1921. There was a fire that destroyed that absorption plant, do you know anything about that?

A No sir.

Q I have here a "History of Alberta Oil" by Messrs. Beach & Irwin. I wonder how much of this information you can tell me as to its accuracy.

MR. CHAMBERS: Pardon me, but just for the purpose of the record. I do not want to be interrupting all the time but I am taking the general objection that as to what took place in the 1920's or in the 1930's, before this Act was passed, is irrelevant and I submit should not be admitted. I am not going to go any further than that because I want to reserve the right to take the objection at another time and place if that should happen.

THE CHAIRMAN: Particularly place.

MR. CHAMBERS: But on the Argument, sir, I want to be free in Argument to say that that should be disregarded and I just want to make that general objection.

MR. STEER: I do not want to introduce anything that is irrelevant, sir. I think perhaps my purpose might be served if my learned friend will agree with a remark which Dr. Boomer made to the Chairman this morning is an accurate one, that this problem which we are facing now is due to the search for oil in this province, that is all. If that is admitted and accepted I need not go any further.

MR. HARVIE: I am not prepared to admit that.

MR. CHAMBERS: I am not prepared to admit it. I am prepared to say this, I do not think it makes any difference to this Hearing whether it is so or not. This Board has got certain duties to perform under the Act that the Legislature passed last year, and as to why the problem was brought about or when I submit has nothing to do with it.

THE CHAIRMAN: We are going to admit the evidence anyway and we will discard that which we find to be irrelevant when the time comes.

Q. MR. STEER: I am reading from page 17, Mr.Mercer, of this History of Alberta Oil by Beach & Irwin and they remark "In the meantime, Mr. A. W. Dingman in 1914 had incorporated Calgary Petroleum Products of which he became managing director." Have you read this?

A I may have read it some time ago, Mr. Steer.

Q "Three wells were drilled and oil discoveries in 1914 precipitated an oil boom. The oil in the three wells of this company was accompanied by considerable gas and was so volatile that experiments were made in recovering the natural gasoline from the natural gas, followed by the construction of a small Absorption Plant." There is not any doubt that there was an Absorption Plant treating gas that came from those three original Royalite wells, or do you know?

A Only from having seen the records.

Q You have seen the records?

A I have never seen the Plant. I never saw the Plant.

Q But you saw the record?

A I think I can say there was a Plant.

Q They were records of the Royalite Company?

A The original records, yes.

Q Is that right?

A I would say yes.

Q From those records you know that statement is true?

A That there was a Plant in existence?

Q Yes. Then this goes on . . . . .

A I might interject, Mr. Steer, that when you say there was a Plant, an Absorption Plant, referring to an Absorption Plant, I do not know whether it had been referred to as an Absorption Plant at that time. There is just a doubt in my mind whether it was.

Q It was a Plant which was intended to extract natural gasoline from this wet gas from those three wells. Is that right?

A Yes it was an extraction plant.

Q Then this goes on:"A fire on October 20th, 1920 burned this Plant and the need of its replacement precipitated the need of refinancing the company. On December 24th, 1920, the shareholders ratified arrangements for refinancing and early in 1921 a new organization known as the Royalite Oil Company took over the assets of the Calgary Petroleum Products and rebuilt the Absorption Plant and started further drilling." Do you know that from the records that you have examined of this Company?

A From what you have read regarding the original plant and having read further, I would not know anything about that original plant. I do know from the old records that there was a Plant, the old original plant of the Royalite.

Q For the purpose of extracting natural gasoline from this wet gas?

A As far as its general purpose was concerned, I would not know what it was used for. But there was a Plant on the records, the original records of the Royalite. It might have been that rebuilt plant that is referred to there.

Q Yes. "Then in the Fall of 1921 a 6 and 8 inch pipeline was laid from the Absorption Plant to Okotoks where it fed the transmission lines to Calgary, gas being turned into the line on December 31st, 1921, after passing through the Absorption Plant and Compressors". I am suggesting to you, Mr. Mercer, that your records will show and if you do not know this I will ask you to search your records and let us know, that the pipeline, that 6 and 8 inch pipline from the Absorption Plant to Okotoks, in the latter part of 1921, was built following a Board Order made by the Board of Public Utility Commissioners directing the Gas Company to augment its gas supply and that in augmenting that supply the Gas Company built this line to connect up with the Royalite Absorption Plant in the latter part of 1921. Are you prepared to make a statement as to whether that is so or not?

A No I cannot make a statement.

Q Then I ask you to find out whether or not that is so and then I ask you to check the order of the Public Utilities Board made in October 1921 on page 5 of that Order where it speaks of residue gas from wells drilled for oil. That the Royalite Company stated or the Imperial stated that they operated a gasoline extraction plant and they had residue gas from wells drilled for oil and they offered to supply that gas to the Gas Company. I suppose you have not any recollection of that.

A No.

Q Then I would ask you to check that.

MR. BLANCHARD: May we have a certified copy of that Order put in, sir?

MR. CHAMBERS: I would like to make my position clear. I do not want to be technical but if there is an Order of the Public Utilities Board that the Gas Company is a party to I submit that should be proved by it being filed here by the Gas Company rather than asking this witness to do it.

MR. STEER: I am asking Mr. Mercer to verify statements from the records, which are the records of the Royalite Oil Company. If necessary to prove it I will prove it by filing the Order.

MR. CHAMBERS: In line with my objection, I take it that this history is not relevant. At the moment I am not prepared to undertake that this witness will do that.

THE CHAIRMAN: It may not be relevant but until Mr. Steer develops what he is developing to a much greater length it is impossible for anyone to say whether it is relevant or not. And to say "No, we will not hear this cross-examination," would be quite wrong.

MR. CHAMBERS: I am not suggesting that. But what I am saying is this witness is being asked to go an do a lot of research and I am suggesting there are other ways in which it can be proved. The Gas Company seems to know all about this and why should not they bring their own witness. I do not want to be obstructive and I want to co-operate but after all to ask this witness to make searches on these things is going very far.

THE CHAIRMAN: I remember when I was in practice - and I perhaps did not have as great a practice as some of you - I always enjoyed very much proving my case out of my opponent's

mouth if I could.

MR. CHAMBERS: But the point comes up that he is not asking the witness a question as to what he knows. There is no obligation, legal or otherwise I submit, on the witness to go and make researches.

THE CHAIRMAN: If counsel says to the witness "are you in a position to get the information?" and the witness says "yes, I am".

MR. CHAMBERS: But he is not obligated to get it.

THE CHAIRMAN: If I say he shall, then he must.

MR. CHAMBERS: Then we have to argue this whole point about the Board's jurisdiction.

MR. STEER: That is the way I understand this Inquiry has been conducted up to date. If this witness has access to that information, under proper direction of the Board he could get the information, just in the same way as every witness, practically every witness before the Board has done up to this time.

THE CHAIRMAN: That is right.

MR. STEER: If necessary, I can prove these things by putting them in.

Q That is pretty much the situation up to the end of 1921, Mr. Mercer, there were those three wells supplying the wet gas and that wet gas was treated for the extraction of naphtha, then I am suggesting to you by Board Order of October 1921 directing the Gas Company to augment its supplies, there came about the agreement of December 1921 between the Royalite Company and the Canadian Western Company under which the Canadian Western Company took this residue gas from that Absorption Plant. You perhaps are not in a position to say yes or no to

that proposition at the moment. I ask you to get the information and let me know tomorrow whether that is so. Then in October, 1924 the Royalite No. 4 became a producer. You know that date, do you?

A Yes sir.

Q And apparently in July of 1925 there was a further agreement between the Royalite Company and the Canadian Western Company with regard to the gas produced from Royalite No. 4 which was in Section 7. Do you know about that?

A There was a further agreement in that year, yes.

Q We will put those agreements in. Now Royalite No. 4 was also drilled, as I understand it, in the search for oil. It was not drilled to find gas was it?

A I am hardly in a position to say why a well was drilled in 1924.

Q I suppose that is so. The records show that almost one million barrels of oil, natural gasoline - I think the records show almost one million barrels of natural gasoline were produced out of that well, do you know about that?

A I can say generally yes. There are records to show that.

THE CHAIRMAN: Up to what date?

MR. STEER: Up to the date of its abandonment. It was abandoned, I believe, in 1934. Am I right in that?

A It was somewhere around there, I do not know offhand what date it was.

DR. BOOMER: That is already in as an Exhibit filed.

MR. STEER: Which?

DR. BOOMER: The Conservation Board records have been filed.

MR. STEER: That is probably so.

Q Now then, my suggestion to you, Mr. Mercer, is that every other Royalite well which was drilled following No. 4 was drilled in a search for oil and that there was not a single one of these wells that was drilled for the purpose of recovering gas. What do you say to that?

A That depends on, as I said in the case of Royalite 4, I did not know the reason for it being drilled, whether it was drilled for oil or not. Certainly your question will hinge on that, Mr. Steer.

Q Irwin & Beach in this report have this to say: - these wells were drilled in Turner Valley, of course?

A In the Turner Valley field, yes.

(Go to page 2602)

Q "The story of Turner Valley and its development is, up to the present, the real story of Alberta oil. It is the story of Canada's oil as well, for, as a result of all that has developed over the last twenty-five years in this small section of southern Alberta, Canada in 1939 took, for the first time in her history, a definite second place amongst the oil producing countries of the British Empire."

Now what I am suggesting to you, Mr. Mercer, is this, that the Turner Valley area is an oil field and is not a gas field, do you agree with that ?

A On a point like that I would not want to voice an opinion Mr. Steer.

Q I see. Well I am afraid we are not going to get any more Royalite people in the box.

MR. CHAMBERS: Call Mr. Beach.

Q MR. STEER: I suppose you would go this far, that, according to all the reading you have done, and the reports you have read, that Turner Valley is an oil field and not a gas field ?

A It is generally referred to as an oil field.

Q Yes, and the extensive drilling which was done in Turner Valley would never have been done if people had not had in their minds the production of oil, is that right ?

A That is so, since 1936 when the first well as an oil well was brought in.

Q Well it was so prior to 1924 when Royalite #4 came in, was it not; these wells, these Royalite #1, #2 and #3 wells, and the drilling which was done in Turner Valley prior to October 1934 was oil drilling, was it not ?

A Certainly the boom, which you spoke of, was referred to as "an oil boom" Mr. Steer.

I N D E X

Volume 33

Sept. 4th, 1945.

WITNESSES	Page
Discussion	2541
R. D. MERCER (Continued)	
Direct Examination.....	2546
Cross-Exam. by Mr. Fenerty.....	2572
Cross-Exam. by Mr. Steer.....	2591
Cross-Exam. by Mr. McDonald.....	2615

E X H I B I T S

No.		
98	Submission by Royalite Oil Company Limited in respect of Cost of Delivering Wet Gas to the Natural Gasoline Plant (R-2).....	2546
99	Submission by Royalite Oil Company Limited in respect of Price to be paid for Gas to be re-pressured or conserved in Turner Valley or Bow Island fields by Royalite Oil Company Limited..	2553
100	Agreement between Royalite Oil Company Limited and Canadian Western Company, 1921.....	2594
101	Agreement between Royalite Oil Company Limited and Canadian Western Company, 1925.....	2594

: : : : :

Q And you are not prepared to say - -

THE CHAIRMAN: Which boom, I know of three.

Q MR. STEER: 1914 is the one mentioned and that we were talking about; now we have in front of us here Exhibit 68, which is the agreement between the Madison and the Royalite Company for the severance of these properties; the agreement is made the 10th of March 1944, but to take effect as I understood it on the 1st of January 1944, is that right ?

A Yes.

Q And the agreement commences with a recital "The Vendor has as part of its business operated a natural gas Department including the gathering, purifying, scrubbing, purchasing and selling natural gas"; the business of the Royalite Company, which is referred to as the Vendor in this Agreement, was one business up to the 1st of January 1944 with a natural gas Department, is that right ?

A Yes, it was part of the whole operation of the Company with that section of it.

Q What other Departments were there besides the natural gas Department of the Royalite business ?

A There would be the Production Department and the Absorption Plant Operation.

Q The Production Department would be the Department charged with the production of crude oil from crude oil wells, is that right ?

A And the necessary natural gas produced.

Q Certainly; the natural gas produced, I will put it to you, is a by product of the production of crude oil ?

A Not necessarily. The Royalite Oil Company did have, in the gas cap area, properties which produced natural gas; that was also

part of the production department.

Q The production of natural gas alone ?

A From the wells located in the gas cap area, yes.

Q Do you mean to say that those wells in the gas cap area which were producing gas alone, were not all connected up with the absorption plant ?

A They were produced as a separate unit.

Q Am I right in saying that you have three departments, - you have the crude oil department where you produce crude oil from crude oil wells with gas as the lifting force, is that right ?

A Yes.

Q You have got an absorption plant which treats gas, wet gas from the wells for the purpose of gathering the natural gasoline content, is that right ?

A It treats all natural gas in the neighbourhood of the absorption plant.

Q It treats the gas from the crude oil wells as well as the gas from the gas cap wells ?

A That is right.

Q Yes, and then in addition to that you have this natural gas department that you speak of in this Agreement, Exhibit 68 ?

A As part of the producing department, yes.

Q The natural gas department is a part of the producing department ?

A I am sorry, I misunderstood you. No, you are quite right, as a separate unit.

Q You sever the crude oil department from the natural gasoline department, do you; how many departments have you, three or two ?

A We have the producing department and the natural gasoline department today.

Q And prior to the 1st of January 1944 you had a natural gas department ?

A That is quite right.

Q And that was all one integrated business ?

A Yes.

Q And the evidence here is that your records were kept in such a way that you cannot segregate costs, at least you did not segregate costs and profits from each of the departments, but you figured your costs and profits on all three departments as one business ?

A That is quite so.

Q That is correct ?

A Yes.

Q When you came to sever the natural gas department from the other two and turn it over to Madison, I suppose you found in some property account or other a record of the properties that were being transferred, did you ?

A That is quite so.

Q And you took out of that property account the items which were being transferred to Madison and the balance represented, - of that property account, - represented the items which were left for the Natural Gasoline Department and the Production Department, is that right ?

A That would be so, yes.

Q Yes, and I suppose that either you or some accountant could now go into that property account and pick out of it all the items of property that were used in connection with the natural gasoline end of the business, is that right ?

A A segregation can be made.

Q MR. STEER: Yes, and I am going to ask that that

segregation be made. I am going to ask the Board to direct that the segregation be made and that there be presented to the Board a record of all the items used in connection with the gasoline business, for the reason that I am going to suggest that the business of the Madison Company must be regarded, under all the circumstances, as an integral part of the gasoline operations of that Company.

MR. CHAMBERS: If the Board pleases, before a direction is made one way or the other, I would like an opportunity to argue the matter and put my submission before the Board. In the ordinary course I would have had it ready this morning. As a matter of fact I had it lined up before the adjournment in June but in the course of my conversations with Mr. Fenerty the other day I got an intimation from him, - not from Mr. Steer, because I took it for granted that Mr. Fenerty was the first man going to raise it, - that he was not going to deal with it at this stage of the proceedings. Now I would like to have that part of the application adjourned until tomorrow and I am prepared to argue it tomorrow morning the first thing. Otherwise I would have been ready.

THE CHAIRMAN: As I understand it, Mr. Steer is asking that a segregation of the, of what you might call "The capital structure" of the gasoline absorption unit be made from the rest of the Royalite structure.

MR. STEER: Yes, and then I go further and I ask, and I was going to ask further for the records of the Royalite Company with regard to the operation of the gasoline end, along with the natural gasoline, for several years back, the revenues which were derived from gasoline and from natural gas, the cost of operation with respect to the gasoline and natural gas - -

MR. FENERTY: And that would include the statement that

Mr. Kirkpatrick referred to, which he told us showed the division of costs in the gathering lines of 60 - 40, 60% to the gas industry and 40% to the natural gasoline, that is one of the things I have been waiting to ask about.

MR. CHAMBERS: It might save time ultimately if we more or less got an understanding now of all these things.

MR. STEER: I think that covers it, but perhaps my learned friend and I might put down in black and white exactly what we want and that might be argued tomorrow morning.

MR. CHAMBERS: And can I get that fairly early this afternoon ?

MR. STEER: Quite so.

Q MR. STEER: I suppose you are familiar with the acquisition of the Royalite Company of quite a large number of gas cap wells, from other companies? ?

A You mean the acquisition of those properties during the thirties Mr. Steer ?

Q Yes.

A Yes, to some extent.

Q And your records will show the cost to Royalite of those properties, and they would show the expenses of operation of them and what the proceeds were of the sales from the properties, for each individual property ?

A It would show the acquisition cost, yes. The direct operating costs, we would have records to show that, the operating costs.

Q Of each individual well ?

A Of each individual well. I say "direct operating costs".

Q Because there are some costs, such as overhead, which are divided ?

A Which have never been distributed.

Q But that is an accounting problem I suppose, the distribution of those, what we may call,"common costs" ?

A It would be an accounting problem.

Q And I suppose you would have those records with regard to every well you operate, whether it was one purchased in that way or whether it was drilled by yourselves ?

A Yes, covering the direct operating costs.

Q Now what costs are there over and above the direct operating costs, - is there anything except office overhead, what is there that would have to be distributed ?

A There would have to be a distribution of gathering costs and administration, overhead, general overhead, costs which would have to be taken into consideration.

MR. STEER: I think perhaps we will give to Mr. Chambers a statement of what we will require in that direction and then it can be settled.

Q MR. STEER: I want now to ask you a question or two on this question of gathering costs; you emphasized several times in answering Mr. Fenerty, "the cost of service" to the Royalite and Royalite cost of service, do you recall that ?

A Yes.

Q Now the Royalite gets from that gathering system the maximum of service, does it not, a very valuable service, - I am suggesting to you that what it gets is a very valuable commodity ?

A Which is delivered to it.

Q Wet gas ?

A Yes.

Q Now wet gas is a commodity, "goods" is it not, in substance ?

A Yes.

Q It has a physical existence ?

A Yes.

Q And at least Royalite in its absorption plant uses that commodity and when the commodity leaves the absorption plant it is a very different thing from what it is when it enters, is that not right ?

A Yes, there has been a segregation and a product obtained.

Q In other words what Royalite has done is to take in wet gas and by a scientific process extract certain parts of that wet gas and discharge the balance from the outlet of the absorption plant, is that right ?

A Quite right.

Q Now then it is not true to say that Royalite gets service only, is it, it gets much more ?

A It would get the same service as any other transportion company would provide to anybody using its facilities.

Q True; if the Royalite bargained for the transportation of that gas into its plant, it would be getting service; Royalite does not do that, does it, on this set up, Madison gets that gas does it not ?

A Yes.

Q At the outlet of the separator,-at the outlet of the well head, does Madison get the gas ?

A Yes, Madison gets it.

Q And Madison transports that gas to Royalite, Royalite takes what it wants out of it and delivers the balance over again to Madison, is that right ?

A That is the operation.

Q Yes; before there was any demand, - I will put it this way, - assuming that there was no demand for that residue product, it is always there, and all would be burned ?

A You mean the dry gas ?

Q Yes.

Q Well that is true. I was thinking back if there had been a demand for that type of product for a good many years.

MR. STEER: Oh surely.

(Go to Page 2611)

Q Now your suggestion is that inasmuch as the volume of gas entering the absorption plant is reduced by we will say 15% as it passes through the absorption plant, that 15% represents the proportionate cost of all these gathering facilities which the Royalite Company ought to bear, is that right ?

A That is so.

Q That is it. I need not labour the point that at one time Officials of your Company thought that an entirely different method of dealing with the segregation of costs should be followed. My friend Mr. Fenerty referred to that this morning and I need not labour the point. I am going to suggest this to you that Royalite could not get along without 100% of that volume of that gas as it comes from these well heads could it, in its absorption plant. It needs it all ?

A Being the carrying force, yes.

Q Being the carrying force ?

A Of the absorption plant product.

Q Yes, exactly.

A The same as it is the carrying force in the recovery of crude oil.

Q I see. So that you do agree with me that the gas is a by product of the gasoline industry, if it is a by product of the crude oil industry. Let us assume that the gas is a by product of the crude oil industry where crude oil is being produced from these wells, do you follow ?

A Yes.

Q And then what I understand you to say that so far as the absorption plant is concerned the residue gas performs the same function with respect to the naphtha content that the gas performs in raising the crude oil ?

A It is still the carrying force, yes.

Q And if gas is a by product of crude oil then it follows necessarily that residue gas is a by product of this absorption plant business. That follows does it ?

A Yes, it follows through.

Q Now there was some discussion about this being a conservation scheme and I was interested in an answer that you gave to the effect that this Statute had been passed for the purpose of conserving gas which would otherwise be wasted. Do you recall making such an answer as that ? I do not know whether you stated the Statute was passed for that purpose but you talked about this gas being wasted and the object being the conservation of it. Perhaps I am not quoting you quite correctly. That is the object of this hearing is it, to conserve a product which would otherwise be wasted ?

A That is my understanding.

Q And the product that would be wasted is the residue gas issuing from the absorption plant of the B. A. Company, the residue gas issuing from the absorption plant of the G. O. P. Company, the residue gas from the absorption plant of the Royalite Company, and any gas that is used for the purpose of lifting crude oil. Those are the things that we are interested in saving, are we ?

A Generally, yes.

Q Now then that being so why are we interested in anything that occurs prior to the outlet of these absorption plants. Have you any suggestion about that ?

A No sir.

Q I take you to the G. O. P. plant. Now there is not any doubt that the gathering lines of that plant were installed for the purpose of bringing wet gas into that plant and treating it and getting natural gasoline out of it, is that right?

A Well of course I have no knowledge of the operations of the G. O. P. but it would follow Mr. Steer.

Q But you do know about the Royalite #2 when it existed down in the south end, don't you ?

A Yes sir.

Q Now Royalite #2 down in the south end did not deliver any gas to the Calgary system at all did it ?

A No, I do not believe it did.

Q And before the union of that plant with #1 plant, the residue gas from your #2 plant in the south end was flared, was it not ?

A Yes sir.

Q Now the gathering lines that connected your #2 plant with the various wells in thatarea were installed for one purpose and one purpose only and that was for the purpose of bringing wet gas into that #2 absorption plant, is that right ?

A That is right.

Q They were installed in no sense for the purpose of gathering any gas other than that ?

A That is correct.

Q Now the B. A. plant I think you know flared its gas at the outlet of its absorption plant. You know that ?

A Yes, I understand that.

Q And the G. O. P. the same. Now those three plants, your #2, and the B. A. and G. O. P. are all natural gasoline plants with no connection whatever with natural gas until this Statute intervened to say gas which had been previously flared had to be conserved. That is right ?

A That follows, yes.

MR. CHAMBERS: Just a moment. Royalite #2 plant was out of existence before this Act was passed.

MR. STEER: Oh yes, I know that, surely. I am talking about conditions as they existed before #2 plant went out of existence.

Q I am suggesting to you Mr. Mercer that if it had not happened that Calgary needed an augmented gas supply years ago, your operations in #1 plant would have been carried on in exactly the same way as they were carried on in #2. What would you say to that ?

A That not having been the case I do not think the hypothesis should be made of that.

Q You do not want to say on that. Perhaps you will say this, your gasoline operations from your #1 plant, gasoline I am talking about now, made a lot more money for the Royalite Company than your gasoline operations from your #2. Didn't they ?

A Different types of plants and I believe greater volumes of gas were handled in #1 plant.

Q And if your Company would build its #2 plant as a gasoline business a fortiori it would have built #1 to have handled a much greater volume and make a great deal more money even if there had not been any demand for gas for Calgary at all. Don't you think that follows ?

A That may have been true. I would not be in a position to answer that proposition.

Q Perhaps that will be a problem of economics. Subject to those questions which we will put down in writing for the witness I think that is all.

MR. HARVIE: I have nothing.

THE CHAIRMAN: No cross-examination ?

MR. HARVIE: No I have nothing.

THE CHAIRMAN: Mr. McDonald ?

MR. McDONALD: Just a few questions.

CROSS-EXAMINED BY MR. McDONALD:

Q If you will refer to Exhibit 99, you referred to the period of fifteen years being the period that gas will be conserved and repressured gas used. What is the attitude of the Royalite Company if it should be determined the fifteen years is a longer period than the evidence adduced at the hearing may warrant ?

A That is something I could not answer offhand Mr. McDonald. It is a matter for Royalite engineers to consider a change in that period.

Q What I am getting at is that your factor .31524 is calculated on fifteen years ?

A That is quite right.

Q And the period during which this gas will be conserved or repressured before it is used is twelve years, your factor would be out would it not ?

A Yes.

Q Then is this a proposal by Royalite is or is it subject to variation by the Board ?

A Royalite has used the time element as previously submitted or to be submitted of thirteen years that repressuring and conservation will be in effect and a further two years before the present gas allowables will not be sufficient to meet the then market demand.

Q Then the market demand as presented in evidence is based on the Alberta Nitrogen Company being in operation for 1945 and for six months in 1946. Now if it should follow that the Alberta Nitrogen Company should be in operation for six months or two years longer the possibility of this repressured gas being used at an earlier period may arise and I want to find out now is there room in this proposal made by Royalite for the Board to fix the period of amortization of these moneys ?

A I am not in a position to say whether any extension of service

by a customer like the Alberta Nitrogen Company will affect the time limit or not. I think it is a matter for the engineers to speak to.

Q Now then this factor of .31524 also is worked out on a basis of 8% interest compounded over the period ?

A That is quite right.

Q What is the attitude of the Royalite Company in the event that the Board should determine 8% is not a fair and reasonable rate of interest. Is that subject to decision of the Board ?

A That would be subject to the deicsion of the Board. The Royalite Board of Directors I might say there Mr. McDonald.

Q That is something you reserve for the consideration of the Royalite Board ?

A Quite.

Q Just dealing with the question of 8% on the first Page of Exhibit 99, Paragraph 3, you refer to some hazards that have a bearing on the fixing of the rate of discount. Have you made any calculation as to the deferred recovery of absorption plant products by Royalite ?

A The latter part of your question please.

Q Have you made any calculation of the losses on deferred that Royalite is not going to receive because of this conserved gas ?

A Not over all, no.

Q You have not ?

A No.

Q May I suggest Mr. Chairman that will have a bearing on the outcome of the question of Mr. Steer for exact operations of the Royalite Company with respect to different wells. I would like to cross examine Mr. Mercer in regard to cost of operation

of the gas cap wells and the wells which are being shut in to conserve gas and that can stand until after that matter has been argued and information furnished.

MR. FENERTY: Would it be convenient to Counsel if you adjourned a quarter of an hour earlier today.

THE CHAIRMAN: Before you argue your motion tomorrow I want the cross-examination of this witness to be finished as far as it can be finished and Dr. Boomer and I will have some questions to ask after Counsel are through and we would like those questions answered before you argue your motion. We will adjourn now.

(The hearing then adjourned until Wednesday September 5th at 9.30 A.M.)